

Customer
Service
Programme-
Europe
(CSP-E)



Strategic Market Directions in Customer Service

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STRATEGIC MARKET DIRECTIONS
IN CUSTOMER SERVICE

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IN CUSTOMER SERVICE

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STRATEGIC MARKET DIRECTIONS IN CUSTOMER SERVICE

ABSTRACT

This report discusses the market forces that are creating a changing market environment for customer services. It describes a number of development scenarios, examining the implications for the growth of software support and other services for vendors faced with slower growth in hardware maintenance revenues. The report describes strategic level options for customer services management.

This report contains 52 pages, including 16 exhibits.

STRATEGIC MARKET DIRECTIONS IN CUSTOMER SERVICE

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I INTRODUCTION

A. OBJECTIVES

- INPUT considers that one of the most significant challenges facing customer service management is the potential erosion of hardware maintenance revenues.
- In response to that challenge management must adopt new approaches to their business and consider fully their potential market impact and contribution to corporate revenues and profit.
- This report is one of three related and complementary reports that address this issue.
- This report, Strategic Market Directions in Customer Service, studies the market forces which are creating a changing market environment for customer services, describes model scenarios of revenue growth development, and describes strategic level options for customer services management.
- Two other related and complementary INPUT reports are:
 - Future Service Market Requirements examines vendor attitudes in respect to changing market directions, and assesses user needs and the tactical responses of vendors to these new opportunities.

- The Role of the Engineer Outside of Maintenance analyses the changing role of the customer engineer as user needs and market forces change, the views of customer service management, and the new demands on customer services personnel.

B. METHODOLOGY

- This report, produced as part of INPUT's 1986 Customer Service Programme in Europe, is based upon INPUT's continuing research studies.
- During 1986 this research activity has included over 300 user interviews conducted by telephone and over 60 vendor interviews performed throughout the year with leading hardware manufacturers and third-party maintenance organisations.
- For this particular series of reports, over 20 vendor interviews were specifically conducted to elicit comments on a variety of topics related to the issue of new services trends in response to the threat to hardware maintenance revenue.
- INPUT would like to express its thanks to all those companies and individuals who participated in the research undertaken for this report.
- Enquiries and comments regarding this report and any related topics of interest are welcomed by INPUT.

C. REPORT STRUCTURE

- The remaining chapters of this report are organised as follows:
 - Chapter II is an executive overview providing a summary of the contents of the entire report.
 - Chapter III describes the changing conditions in the marketplace for customer service and the threats to service revenues.
 - Chapter IV discusses the vendors' response to these threats and analyses the classification of revenues within the customer services business.
 - Chapter V describes a model of the development of customer services hardware maintenance revenues and examines some possible scenarios that result.
 - Chapter VI examines the strategic approaches that are open to customer services management, including the development of market opportunities, market leadership, specialisation, and divestment strategies.

II EXECUTIVE OVERVIEW

- This Executive Overview is designed in a presentation format in order to:
 - Help the busy reader quickly review key research findings.
 - Provide a ready-to-go executive presentation, complete with script, to facilitate group communication.
- The key points of the entire report are summarised in Exhibits II-1 through II-6. On the left-hand page facing each exhibit is the script explaining its contents.

A. THE CHANGING MARKETPLACE FOR CUSTOMER SERVICE

- There are a number of threats to service revenue and these can be conveniently considered as three broad groups:
 - Increasing resistance on the part of users to current levels of maintenance charges as they perceive maintenance services to be increasingly unnecessary and 'impersonally' provided.
 - Increasing competition from independent specialist maintenance companies (or TPMs) and from the value added resellers through whom increasing amounts of equipment are being channeled.
 - The increasingly inherent reliability of computer equipment and the trend towards more efficient methods for fault diagnosis.
- The vendor response to these changes has basically been to consider new opportunities for developing additional customer services revenues.
- Through the enhancement of existing services and the development of new services in related or adjacent areas of the business, vendors seek to make up for any shortfall in hardware maintenance revenues.

THE CHANGING MARKETPLACE FOR CUSTOMER SERVICE

- **Revenue Threats**
 - **Customer Resistance**
 - **Competition**
 - **Reliability**
 - **Vendor Response**
 - **Seek New Opportunities**
 - **Enhance Services**
-

B. MARKET DEVELOPMENT SCENARIOS

- Most customer services managers are anticipating overall growth for customer services revenues of at least 10% per annum.
- In this study INPUT developed a number of scenarios in order to examine the implications on overall customer services revenue growth of the hardware services component.
- These scenarios are dependent upon how optimistic or pessimistic the expectations are regarding the growth of the hardware maintenance component.
- The scenarios showed variations in hardware maintenance revenue growth ranging from 8% for the most optimistic assumptions to -1% for the most pessimistic.
- These indicate that increasingly ambitious growth rates will be required from the growth of software support and other service revenues.
- The most optimistic assumptions required software and other service revenues to grow at 17% per annum to achieve an overall service revenue growth of 10%.
- The most pessimistic set of assumptions showed that software and other service revenues would have to grow at 39% per annum in order to compensate for a 1% per annum decline in hardware service revenues.

MARKET DEVELOPMENT SCENARIOS

- **Growth Expectations (AAGR)**
 - **Overall 10%+**
 - **Hardware Maintenance, 8% to -1%**
 - **Software Support and Other Services, 17% to 39%**

C. STRATEGIC APPROACHES

- In the light of forecast market development prospects, the challenge for customer services management is the selection of strategic approaches most suitable for the particular circumstances of the firm.
- In those areas of the market where growth opportunities are identified, the additional challenge is the adoption of marketing initiatives designed to exploit them. This is a market growth strategy.
- Where insufficient growth is expected to meet corporate financial goals, a number of other strategic approaches can be considered. These can be classified as:
 - A market leadership strategy.
 - A specialisation strategy.
 - A controlled withdrawal strategy.
 - A divestment strategy.

STRATEGIC APPROACHES

- **New Opportunity Initiatives**
 - **Market Leadership**
 - **Specialisation**
 - **Controlled Withdrawal**
 - **Divestment**
-

D. MARKET OPPORTUNITY IDENTIFICATION

- When evaluating potential new market opportunities, four basic strategic options can be defined:
 - Market penetration.
 - Service development.
 - Market development.
 - Diversification.
- A market penetration strategy places emphasis on securing and extracting increased revenues from the existing base; for example, with price increases or extended warranty agreements.
- A service development strategy implies the provision of new services to the existing installed base; for example, single-source maintenance agreements, software support, and consultancy.
- Moving fully into third-party maintenance and supporting equipment such as factory automation systems, which is not directly related to existing services, would constitute a market development strategy.
- When completely new services are offered into these new markets, then the strategy would be termed diversification. This is clearly the area that represents the highest level of risk for customer services management.

MARKET OPPORTUNITY IDENTIFICATION

	EXISTING SERVICES	NEW SERVICES
EXISTING MARKETS	PENETRATION	SERVICE DEVELOPMENT
NEW MARKETS	DEVELOPMENT	DIVERSIFICATION

E. POSITIVE STRATEGIES

- Where a decline in the overall market is anticipated, positive strategies for remaining in the market as an active player are:
 - Market leadership.
 - Market specialisation.
- Market leadership implies aggressive moves to obtain market share and thus to manoeuvre into a position of market control.
- Creating economies of scale in service operations leads to above average profitability; hence, the strategy of lowest cost producer wins.
- Positive action to obtain market share through acquisition approaches, thus effectively lowering the exist barriers for weaker competitors, is key to the implementation of this strategy.
- A specialisation strategy, in contrast, is one in which a market niche is selected in some area of the business which is considered reasonably stable.
- A company selecting this approach must carefully evaluate its own strengths and match these against those required for success in the targeted niche markets.

POSITIVE STRATEGIES

- **Market Leadership**
 - **Market Share**
 - **Economies of Scale**
- **Market Specialisation**

F. WITHDRAWAL STRATEGIES

- A company may decide that it wishes to withdraw completely from a market where growth prospects are limited. Increasing competitiveness from strong players and poor profitability may lead it to seriously evaluate this possibility.
- If this is the case, there are basically two alternatives:
 - To target a long-term withdrawal from the market--a controlled divestment.
 - To plan for early divestment.
- Controlled divestment, to be successful, implies a determined exploitation of the existing business in order to extract maximum profitability in the short term. This will probably imply severe limitation of the service provided and its range, including the elimination of smaller less profitable customers.
- In the long term, the penalty of customer dissatisfaction leads to the eventual termination of the business.
- Divestment of the business earlier rather than later is a strategy predicated on the judgement that the optimum price can be obtained for the business before further decline lowers the value of the business.

WITHDRAWAL STRATEGIES

- **Controlled**
- **Early Divestment**

III THE CHANGING MARKETPLACE FOR CUSTOMER SERVICE

- The research conducted for this study indicated clearly that customer services management consider hardware maintenance revenues to be under threat.
- About one-half of the vendors interviewed are in the process of developing aggressive plans for generating revenue within the overall customer services operation from services and activities other than pure hardware maintenance and repair.
- The remainder, who considered their role to be exclusively the support of installed products sold by their product marketing operations, foresee changes in their business that are vital if they were to respond to customer resistance and competitive pressure. Changes such as:
 - More flexible contracting procedures.
 - Limited diversification of activities.
 - Increased marketing and promotion.
- The threat to service revenue can most conveniently be classified into three broad groupings which are discussed separately below:
 - Customer resistance.

- Competition.
- Reliability.

A. CUSTOMER RESISTANCE

- Vendors are becoming aware of increasing customer resistance to the payment of 10-12%, on average, of product value for maintenance services. It appears that users perceive many basic hardware maintenance services to be unnecessary and, when required, are becoming more 'impersonally' provided.
- The tendency towards impersonal maintenance services will bolster resistance amongst users to paying maintenance charges where the service is not entirely visible to them. As one user remarked, 'Manufacturers should change their approach to pricing and vary it according to the number of engineer visits and not charge a fixed maintenance price'.
- Customers are better informed and know that their systems and components are inherently more reliable as well as cheaper and smaller.
- The users are becoming increasingly aware that they can cover many of the risks of failure themselves, either by buying resilience through redundancy or taking advantage of carry-in, swap, and repair facilities.
- INPUT's user research has typically thrown up such user comments as:
 - 'The price we pay is very high compared to the service we receive'.
 - 'As the price of hardware is falling so should the price of maintenance'.
 - 'It is not good value for what is offered'.

B. COMPETITION

- Increased competition in customer service is being manifested in two principal directions:
 - Firstly, customers are aware of the availability of independent specialist maintenance companies (see INPUT's report Third-Party Maintenance in Europe).
 - Secondly, the rapid increase in product distribution through value-added channels. These include, for example, computer dealers, OEMs, value-added resellers, and other organisations that perform a role in an ever more complex chain of distribution between the original manufacturer and the ultimate consumer.
- These organisations have the ability and resources to set up customer service operations that can effectively perform various levels of service, albeit in some instances on a shared maintenance basis.
- The result is that the customers are becoming increasingly aware that they are in a stronger bargaining position and that they can therefore expect more for each dollar they spend.

C. RELIABILITY

- The third major factor is the changing nature of the products themselves, already referred to above as one of the factors contributing to customer resistance to maintenance charges.

- Inherent reliability, lower unit prices, and the tendency for more built-in capabilities for fault diagnostics are all having an impact on the customer engineering environment.
- New design approaches, enabling simple board or component swapping, are also leading to a justifiable perception of 'fault-free' systems.
- Further, technical developments such as optical disk and laser technology, which are replacing installed equipment that has significant mechanical content, are also aiding this trend.

IV VENDOR RESPONSE

A. THE NEW OPPORTUNITY CHALLENGE

- To date the response of equipment manufacturers to these threats has been mixed. Whilst a majority of vendors interviewed were committed to changes in their maintenance operations, a substantial minority were still almost exclusively concerned with the support of hardware.
- The majority, however, are concerned with establishing third-party maintenance capabilities and diversifying field service operations into other support and even sales assignments.
- One observation that INPUT has made from the vendors interviewed is their concern over their own individual share of the total market.
- INPUT has observed that some companies have a more confident view of the future than others. It is no coincidence that these companies tend to be those without a base of mainframe equipment--the sector forecast to grow at the slowest rate, if at all--over the next few years.
- In contrast those companies that have a greater emphasis on smaller systems and specialised terminal equipment, particularly in the retail and financial sectors, are experiencing significant growth.

- It is interesting to note that the customers' perception of the value of maintenance in these sectors is much greater than for the market as a whole. Thus, there is a much greater willingness on the part of the user to enter into a maintenance contract and with much less sensitivity to price.
- Overall, however, INPUT observes that the most prevalent response from those interviewed amongst the system vendors was one of concern for the future development of customer service revenues.
- The majority of companies that INPUT talked to are set upon a process of increased direct selling activity, aggressive competitive moves aimed at capturing some proportion of the maintenance revenues of their competitors, and diversification.
- These basic tactical moves are discussed more fully in one of the companion reports that resulted from this study--Future Service Market Requirements.

B. REVENUE CLASSIFICATION

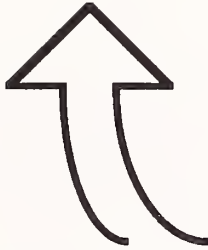
- Currently, most customer services organisations classify their total revenues as being derived from at least three service elements:
 - Hardware maintenance.
 - Systems software support.
 - Consulting services, such as:
 - Site and installation planning.
 - Training.
 - Performance evaluation.

- On average, INPUT calculates that the percentage contribution of each element is as follows:
 - Hardware maintenance - 84%.
 - Systems software support - 10%.
 - Consulting services - 6%.
- A significant minority of companies also include other returns in their revenue totals, principally:
 - Product and supplies marketing, including:
 - . Cabling.
 - . Consummables.
 - . Spares.
 - Applications software.
- Even for this group, hardware maintenance still represents some 75% of total revenues and other sales less than 6% of the total.
- In respect to the age analysis of the hardware installed base, in most cases 75% of the total maintenance yield is derived from equipment that is between two and five years old.
- Only about 7-8% of maintenance yield derives from equipment that is greater than five years old.

- Continuing increases in the rate of change within product ranges is leading to an increasing rate of obsolescence and thus to increasing vulnerability for the most significant segment, that of equipment between two and five years old.
- One respondent estimated that as much as 50% of total hardware maintenance revenue was obtained from equipment that could be considered obsolescent. The users of such equipment would be best advised to replace it with systems that in many cases would cost less than the maintenance cost of the older variant.
- Thus, despite the relative security and predictability of maintenance revenues, there exist potential threats inherent in their source. These are causing management to review future plans and seek to implement approaches that reduce their reliance upon hardware maintenance revenues.
- The more cautious, and possibly more realistic companies, are expecting changes in the contribution of the installed base to take place relatively slowly.
- They believe that the inertia of the market allied to increasing product sales volume will cushion them against any dramatic shift in revenue generation.
- Thus, there are a number of opposing forces, market drivers, and market inhibitors that are influencing the development of the hardware maintenance market. They are depicted in summary form in Exhibit IV-1.
- An assessment of future market potential can only be arrived at after careful examination of these various opposing factors.
- This issue is more fully explored in Chapter III of the companion report Future Service Market Requirements.

EXHIBIT IV-1

MAINTENANCE MARKET GROWTH FACTORS



POSITIVE FACTORS

- Increased Unit Volume
- Customer Dependency
- Enhanced Service Levels

THE MAINTENANCE MARKET

NEGATIVE FACTORS

- Product Reliability
- User Cost Consciousness
- Increased Competition



V MARKET SCENARIOS

- This section examines in more detail the growth expectations of vendors to customer services revenues, and develops a market model that can be used as the basis for scenarios of the market.

A. GROWTH EXPECTATIONS

- It was clear to INPUT from its research amongst vendors that in broad terms nearly all customer services management are expecting that hardware maintenance revenue will represent a declining proportion of total revenue over the next three to five years.
- Some expectations are that hardware maintenance should only represent 50% of total services revenue within five years (e.g., by 1991), down from the reported 84% today.
- At the same time, nearly all customer services managers reflect their companys' expectations that total revenues for customer service should continue to grow, probably by at least 10% per annum.
- In order to gain some realistic insights into the future pattern of customer service revenue growth, a simplified model of the market has been developed.

- The implications of growth expectations can then be examined in the light of the assumptions input to the model.
- The reader can naturally apply different parameters to the calculation in order to evaluate their effects on future market growth.

B. MODEL ASSUMPTIONS

- The market model is described in Section C and the assumptions made in its development are defined below.
- The model is constructed around a 'base year', which could, for example, be considered as 1986.
- In order to develop a formulation of maintenance market revenues for the 'base year', the following assumptions were made:
 - Equipment is retired from the installed base at the following percentage rates:
 - . From first installation through to 'base year-3' = 0% (no retirement).
 - . 'Base year-4' = 10%.
 - . 'Base year-5' = 20%.
 - . 'Base year-6' = 50%.
 - . 'Base year-7' = 80%.
 - . Prior years = 100%.

- Total market product sales in 'base year-7' were 100 monetary units.
 - The growth in the product sales maintained an annual average rate of 15% for the first five years from 'base year-7', falling to 10% in the last two years prior to the base year.
 - The maintenance yield represents 10% of the value of the installed equipment.
 - Price inflation on maintenance averaged 5% per annum in the seven-year period up to the base year.
 - A factor of 50% is applied to the maintenance derived in the first year of installation to compensate for the expectation that actual installations will be spread throughout the year.
- These assumptions are embodied in the model to derive a total maintenance market value for the base year, as shown in Exhibit V-1.
 - In Exhibit V-1:
 - Column i shows product sales for the market commencing at 100 units in 'base year-7' and increasing at an average annual growth rate (AAGR) of 15% and then at 10% for the last two years.
 - Column ii indicates the initial maintenance revenue derived from the product sales in each year at 10% of the 'if sold' value.
 - Column iii shows the effect of 5% per annum price inflation on those maintenance revenues calculated for the base year.
 - Column iv shows the application of the assumptions made about the rate at which installed equipment is retired from the field. It is also

EXHIBIT V-1

MARKET MODEL - REVENUE DEVELOPMENT TO BASE YEAR

YEAR	PRODUCT SALES (VALUE UNITS)	MAINTENANCE REVENUE*		
		INITIALLY	EFFECT OF PRICE INFLATION	IN BASE YEAR
COLUMN	i	ii	iii	iv
-7	100	10	14	3
-6	115	11.5	15	8
-5	132	13.2	17	14
-4	152	15.2	18	16
-3	175	17.5	20	20
-2	201	20.1	22	22
-1	221	22.1	23	23
Base Year	243	24.3	24	12
Total Maintenance Revenues in Base Year				118

*Some figures are rounded.

assumed that equipment sold during one year does not generate maintenance revenue until the following year and that it is only serviced for 50% of that year.

- The market model described in Exhibit V-1 also includes the assumption that up to the base year all equipment installed in the field is covered by a maintenance agreement.

C. MODEL SCENARIOS

- Having established the 'base year' position, it is then possible to develop some future scenarios based upon different assumptions about future developments.
- The three most critical parameters regarding future growth are:
 - The future level of product growth in value terms.
 - The level of maintenance yield, currently assumed to be 10%.
 - The proportion of equipment that is expected not to be needed or covered by maintenance.
- Four scenarios are thus developed in Exhibits V-2 through V-5 that have been calculated on the following set of assumptions:

<u>Scenario</u>	<u>Product Sales Growth</u>	<u>Maintenance Yield</u>	<u>Proportion of Maintenance Equipment</u>
1	10%	10%	100%
2	5%	10%	100%
3	5%	declines to 5%	100%
4	5%	declines to 5%	declines to 75%

EXHIBIT V-2

MARKET MODEL - SCENARIO 1

YEAR	PRODUCT SALES (VALUE UNITS)	MAINTENANCE REVENUE*		
		INITIALLY	EFFECT OF PRICE INFLATION	IN YEAR BASE +5
COLUMN	i	ii	iii	iv
-2	201	20.1	22	4
-1	221	22.1	23	12
Base Year	243	24.3	24.3	19
+1	267	26.7	26.7	24
+2	294	29.4	29.4	29
+3	323	32.3	32.3	32
+4	356	35.6	35.6	36
+5	391	39.1	39.1	20
Total Maintenance Revenues in Base Year +5				176

*Some figures are rounded.

EXHIBIT V-3

MARKET MODEL - SCENARIO 2

YEAR	PRODUCT SALES (VALUE UNITS)	MAINTENANCE REVENUE*		
		INITIALLY	EFFECT OF PRICE INFLATION	IN YEAR BASE +5
COLUMN	i	ii	iii	iv
-2	201	20.1	22	4
-1	221	22.1	23	12
Base Year	243	24.3	24.3	19
+1	255	25.5	25.5	23
+2	268	26.8	26.8	27
+3	281	28.1	28.1	28
+4	295	29.5	29.5	29
+5	310	31.0	31.0	16
Total Maintenance Revenues in Base Year +5				158

*Some figures are rounded.

EXHIBIT V-4

MARKET MODEL - SCENARIO 3

YEAR	PRODUCT SALES (VALUE UNITS)	MAINTENANCE REVENUE*		
		INITIALLY	EFFECT OF PRICE INFLATION	IN YEAR BASE +5
COLUMN	i	ii	iii	iv
-2	201	20.1	22	4
-1	221	22.1	23	12
Base Year	243	24.3	24.3	19
+1	255	23	23	21
+2	268	21	21	21
+3	281	20	20	20
+4	295	18	18	18
+5	310	16	16	8
Total Maintenance Revenues in Base Year +5				123

*Some figures are rounded.

EXHIBIT V-5

MARKET MODEL - SCENARIO 4

YEAR	PRODUCT SALES (VALUE UNITS)	MAINTENANCE REVENUE*		
		INITIALLY	EFFECT OF PRICE INFLATION	IN YEAR BASE +5
COLUMN	i	ii	iii	iv
-2	201	20.1	22	4
-1	221	22.1	23	12
Base Year	243	24.3	24.3	19
+1	255	23	23	20
+2	268	21	21	19
+3	281	20	20	17
+4	295	18	18	14
+5	310	16	16	6
Total Maintenance Revenues in Base Year +5				111

*Some figures are rounded.

- In calculating the future model, price inflation is assumed to be zero and thus all calculations represent real monetary units in the base year.
- It can be seen that these four sets of varying assumptions provide four different scenarios of growth, as shown in the following table:

<u>Scenario</u>	<u>Total Maintenance Revenues in Base Year +5</u>	<u>AAGR</u>
1	176	8%
2	158	6%
3	123	1%
4	111	-1%

- When these forecasts are applied against vendor expectations of overall customer services growth and the percentage represented by hardware maintenance, as described in Section A above, the implications are as tabulated in Exhibit V-6.
- From this exhibit it can be seen that within the overall 10% growth expectation, there are implied very large growth rates for the expansion of other services. These range from 17% AAG for Scenario 1 up to very nearly 40% for Scenario 4, the most pessimistic.
- Given the doubts concerning overall market growth in the computer industry, vendors are recommended to carefully study their future plans in the light of these guideline scenarios.

EXHIBIT V-6

**IMPLICATIONS FOR SOFTWARE SUPPORT AND
OTHER CUSTOMER SERVICES REVENUE GROWTH**

Scenario	CUSTOMER SERVICES REVENUES						Software and Other AAGR
	BASE YEAR			BASE YEAR +5			
	Hardware	Software and Other	Total	Hardware	Software and Other	Total	
1	118	22	140	176	49	225	17%
Percent	84%	16%	-	78%	22%	-	
2	118	22	140	158	67	225	25%
Percent	84%	16%	-	70%	30%	-	
3	118	22	140	123	102	225	36%
Percent	84%	16%	-	55%	45%	-	
4	118	22	140	111	114	225	39%
Percent	84%	16%	-	49%	51%	-	

VI STRATEGIC APPROACHES

- Customer services management must, in the light of the market development scenarios outlined in the previous chapter, assess the strategic approaches that are available to them.
- One of these approaches is clearly the identification of new market opportunities. Either it is considered that there is sufficient growth in the existing market to expand the business or that expansion into new opportunity areas is necessary to make up for the decline in traditional areas.
- These situations are discussed in Section A below.
- Other strategic approaches to the challenge of managing customer services operations in today's difficult environment include more radical options. These, which are discussed below in Section B, include:
 - A market leadership strategy.
 - A specialisation strategy.
 - A controlled withdrawal strategy.
 - A divestment strategy.

A. NEW OPPORTUNITY IDENTIFICATION

- Any organisation is continually faced with the generic problem of new markets and product/service opportunity identification.
- As far as markets are concerned, an organisation can either remain in its existing markets or attempt to sell into new ones. On the product/service side, it can either consider marketing activities to promote existing products or services or be considering new products and services.
- Thus, four basic strategic options can be defined:
 - Market penetration.
 - Service development.
 - Market development.
 - Diversification.
- These basic strategic options are described in the market/product service table in Exhibit VI-1.
- The challenge is a relatively new one for customer services as its traditional protected markets come under new pressures as described in this report (see Chapter III).
- The strategic options for customer service are clearly limited by the particular characteristics of the computer equipment maintenance markets.
- Each one of these four basic approaches is discussed in turn below.

EXHIBIT VI-1

**MARKET OPPORTUNITY IDENTIFICATION
MARKET/SERVICE TABLE**

	EXISTING SERVICES	NEW SERVICES
EXISTING MARKETS	MARKET PENETRATION	SERVICE DEVELOPMENT
NEW MARKETS	MARKET DEVELOPMENT	DIVERSIFICATION

I. MARKET PENETRATION

- At first sight, this area offers the least obvious scope for business development since the market is largely defined by the installed base of equipment supplied by the manufacturer.
- However, there are tactics that can be adopted by the customer services organisation that can lead to increased revenues being generated from the installed base. These are more fully described in the companion report Future Service Market Requirements. Essentially they comprise:
 - Emphasis on continued viability of older installed equipment in order to maintain existing revenue streams as long as possible.
 - Ensure maximum prices for existing equipment covered by maintenance agreements.
 - Develop the concept of extended warranty.

2. SERVICE DEVELOPMENT

- Service development strategies encompass a range of activities that many companies are actively pursuing. These include:
 - The maintenance of other vendors' equipment (single-source maintenance agreements).
 - The provision of other computer services, such as:
 - Software support.
 - Applications systems development.

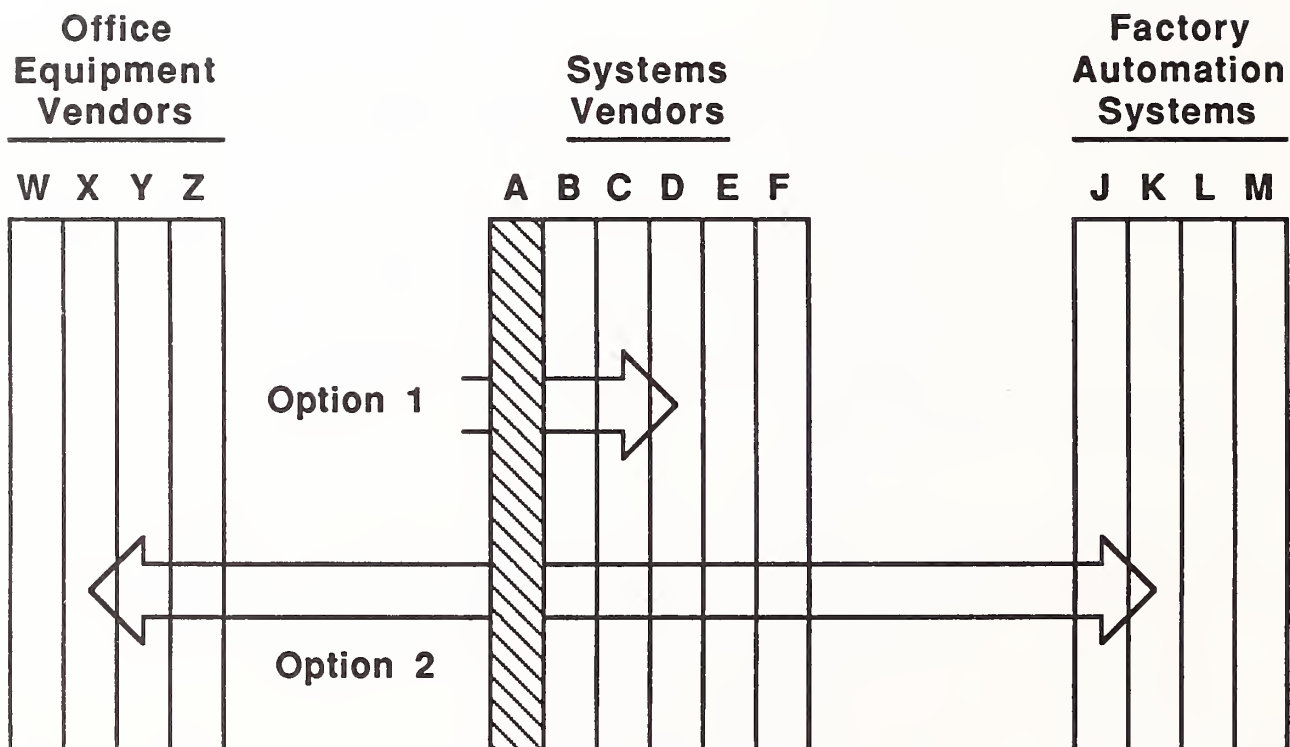
- . Consultancy.
- . Installation planning and implementation.
- The sale of other products through a single sales and marketing structure.
- These development tactics are discussed more fully in Future Service Market Requirements, one of two companion studies to this report.

3. MARKET DEVELOPMENT

- Clearly, the provision of third-party maintenance (TPM) services represents an important market development strategy.
- As well as covering similar products, there is the opportunity to extend these services to different categories of products. For example, from computer systems to factory automation systems and office equipment. This is depicted schematically in Exhibit VI-2.
- The skills required of customer service engineers are increasingly moving towards board or component level fault diagnosis, and these skills could be applied to an increasingly wide range of products incorporating microprocessors and other electronic equipment.
- It is unlikely that it would be effective to consider direct selling to end users of these unrelated products. However, negotiations with the manufacturers themselves could result in licensed agreements or the acquisition of a contracted base.
- Thus, Exhibit VI-2 depicts not only the development of TPM services (Option 1) but the concept of market development of customer services over a wider range of products within a given geographic area (Option 2). This

EXHIBIT VI-2

MARKET DEVELOPMENT STRATEGIES



process should naturally generate economies of scale with regard to the whole operation.

- Another dimension of market development is to consider the extension of geographic coverage of all of these different service elements.
- With the increasing convergence of computer technology into other areas, notably communications, not only is there increasing justification for the computer customer service operation to adopt a market development strategy but increasing need in many instances for it.
- Increasing reliance is being placed upon critical computer-based systems in such areas as banking and computer integrated manufacturing systems.
- Under these circumstances high levels of system availability are of increasing importance and it is these 'critical' application areas which will provide opportunities for high level maintenance service providers.
- Users in these situations are prepared to pay a significant premium. Vendors that can really provide very short response times to urgent demands will be in a position to offer this final added value level of 'insurance'.

4. DIVERSIFICATION

- This strategy embodies the concept of offering new products and services and offering them into new geographic or product areas.
- Clearly, this is a strategy that involves the most risks since it implies the highest number of new variables.

B. STRATEGIC OPTIONS

- Whilst the most obvious consequence of downward pressure on the existing revenue base is the seeking out of new opportunities, as described above, it is not the only option available to management.
- Where a decline in the overall market is anticipated, management can adopt any of the following broad strategic approaches towards the business:
 - Market leadership.
 - Specialisation.
 - Controlled withdrawal.
 - Divestment.

I. MARKET LEADERSHIP

- Sometimes referred to as the 'end game' strategy, the basic idea is for the company to develop a leadership position in terms of market share such that it is able, as far as possible, to dictate terms within the market.
- Creating sufficient scale of operations regionally, nationally, or internationally to support all the required levels of maintenance support is increasingly difficult for any single company.
- Service management is constantly aware of the need to create sufficient scale of maintenance activity in any geographic area to support the required manpower levels and enable call priority assignments to be successfully managed.

- Thus, a valid strategy is to buy into maintenance markets either currently held by independent companies (TPMs) or even for other electronic-based but non-computer system product vendors.
- The market leadership strategy is aimed at achieving economies of scale and, therefore, above average profitability in comparison to the other competitors in the field. In effect the strategy of lowest cost producer wins.
- Some of the principal economies of scale would relate to the following:
 - Increased operational scale at field level.
 - The potential to develop and maintain the most cost-effective logistical management system for call monitoring and parts distribution.
 - The development of systems for statistical management of maintainability for given products and sites most efficiently spread over a wide product and vendor base.
 - The potential to use customer service personnel over a wider diversification of tasks offering increased development and promotion possibilities.
- Some typical tactical steps that can be employed in achieving the objectives of a leadership strategy are listed in Exhibit VI-3.
- Fundamentally, these imply aggressive acquisition approaches basically aimed at lowering the exit barriers for weaker competitors who would be desirous to leave the market if the exit barriers became sufficiently low.

MARKET LEADERSHIP - TACTICAL APPROACHES

- **Actions designed to drive weak competitors from the market.**
 - **Agressive pricing**
 - **Marketing activity**
- **Acquisition of competitors or competitors service business.**
- **Other exit barrier reduction tactics.**
 - **Provision of spare parts, possibly through manufacture**
 - **Taking over long-term contracts**
 - **Provision of logistical support to competitors**
- **Developing 'lowest cost' service provider status by investing in state-of-the-art methods that simultaneously raise the stakes for other competitors to stay in the business.**
- **Orchestrate a marketing campaign designed to demonstrate commitment to the business and at the same time put off competitors from unrealistic assessments of the markets future prospects.**

2. SPECIALISATION

- A specialisation strategy demands a fundamental assessment of a company's strengths.
- Given strengths in a particular area then, the consequent strategy demands the development of a strong position in that area.
- Of course a company can deliberately set out to develop the particular required strengths following an assessment, not so much of what strengths the company already has but what strengths are required for survival in the marketplace.
- Clearly, those market areas most suitable for specialisation or niche strategies are those where demand is considered most stable.

3. CONTROLLED WITHDRAWAL

- In some instances a firm can choose to reduce investment in the business to a minimum and to continue on a care and maintenance basis.
- In this situation such tactics as the elimination of small less profitable customers, limiting the provision of services to the bare minimum, and limiting the range of products serviced are all to be considered.
- Taken beyond a commitment to remain in some selected market niche, this kind of strategy ultimately leads to disengagement from the business.
- The evident rationalisation that is taking place amongst computer equipment manufacturers and other related businesses is often referred to as the industry 'shakeout'.

- INPUT believes that it is inevitable that the increasing demands for investment in providing customer services will not only contribute to further 'shakeout' in the industry but lead to new formations and structures within the services industry itself.

4. DIVESTMENT

- Given the increasing threat of further shakeout in the industry and the need for increasing investment to stay competitive, a valid strategy for some operators will be divestment.
- The premise in this approach is based on a long-term assessment of the future trends and a decision to exit from the business earlier rather than later.
- Divestment of the business, enacted early on in a declining market situation, can usually optimise the financial value that the company can obtain from the sale of the business.
- The key challenge for management in this situation will be facing up to the exit barriers. Companies in this position will most likely need to seek out organisations bent on a market leadership strategy to whom they can sell the business.
- Maintenance services are potentially very profitable if all the business components are balanced optimally. They are, therefore, an attractive option to companies with an existing high value product installation base.
- There exist companies that will want to expand their activities. Those operating a market leadership strategy, for example, are likely to be potential purchasers of existing maintenance businesses.
- The potential to realise significant immediate capital inflows and escape the problems of managing an increasingly less profitable business can be an attractive option for some vendors.

About INPUT

INPUT provides planning information, analysis, and recommendations to managers and executives in the information processing industries. Through market research, technology forecasting, and competitive analysis, INPUT supports client management in making informed decisions. Continuing services are provided to users and vendors of computers, communications, and office products and services.

The company carries out continuous and in-depth research. Working closely with clients on important issues, INPUT's staff members analyze and interpret the research data, then develop recommendations and innovative ideas to meet clients' needs.

Clients receive reports, presentations, access to data on which analyses are based, and continuous consulting.

Many of INPUT's professional staff members have nearly 20 years' experience in their areas of specialization. Most have held senior management positions in operations, marketing, or planning. This expertise enables INPUT to supply practical solutions to complex business problems.

Formed in 1974, INPUT has become a leading international planning services firm. Clients include over 100 of the world's largest and most technically advanced companies.

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